

Briefing Paper 14

Economic analysis and the third sector

Andrea Westall, Associate Fellow, Third Sector Research Centre

Introduction

Part of the reasons for the emphasis on economic analysis by the Third Sector Research Centre, reflects the need for rigorous, credible and generalisable evidence. For example, the Office of the Third Sector is particularly interested in comparable statistics that place the third sector firmly within, and contributing to, the mainstream economy. This need has a practical basis in determining the relative requirement for public money and policy attention.

However, it is important not to automatically equate 'rigour' with economic analysis since other forms of analytical technique or cross-disciplinary approach can be rigorous in their own terms. Equally, economic analytic techniques or conceptual categories in common use may be more or less appropriate to different dimensions or types of third sector activity.

The 'third sector' itself, could be seen primarily as an economic category, often compared in economic models (as non-profit) with for-profit activities and government. This distinction informs much academic work (particularly from the US) but its limits are increasingly being addressed by academic thinkers and challenged by third sector activities and organisations which cross boundaries and blur accepted 'distinct' motivations or attributes (for example, through forms of social enterprise and social entrepreneurship).

As such, a more thorough understanding of third sector impacts and practices, as well as related individual and group behaviour, could itself influence and change mainstream economic assumptions and practice.

So what is economic analysis?

Economic analysis might generally be seen as the tools, concepts, models and theory for understanding, predicting and generalising economic (and other) phenomena. There is an implicit assumption within the use of language and scholarly divisions or practice that 'economic analysis' reflects a different or particular form of lens and approach, to 'other' analytical methods. There is also an assumption that there is one form of such analysis.

The scope and understanding of the relationship and applicability of economic analysis to the activities of the third sector, however, differs according to the views, preoccupations and discourse of particular groups such as government, business, and academia. But it is always important to bear in mind the popular and hence powerful impact of the language, dimensions and assumptions, of a particular and simplified economic analysis. It could also be argued that this narrow view itself has had a reflexive impact on reality (including the conceptualisation of the 'third sector' itself) as well as limiting the implicit understandings around economic terms.

Government view/s of economic analysis relevant to the third sector

We can look at two different but interconnected ways of seeing economic analysis within government discourse and practice. The first relates to the need to justify the importance of policy and intervention towards the third sector relative to other parts of the economy. The second approach relates to the methods of analysis used within government to explore and justify policy interventions and the relative preference for different options.

The ideal implications and operationalisation of economic analysis for day-to-day policy-making are encapsulated in what is known as the *Green Book* which sets out the rationales for policy intervention – those of market failure and equity “ as well as option appraisal using a variety of different cost-comparison techniques.

The *Green Book's* additions and caveats to particular economic analytic techniques (for example, that of Multi-Criteria Analysis (MCA) when dealing with non-monetary impacts) suggest limitations to this approach. Such problems may be particularly true in third sector analysis where many aspects of activities and motivations do not fit with (at least mainstream) economic assumptions or modelling techniques. Neither does third sector policy fit into easy rationales such as ‘market failure’ or ‘equity’.

Academic research on the third sector

The starting point for much US-focussed economic research has been mainstream economic analysis (generally focused on neo-classical approaches and mathematical models), albeit with refinements and attempts at increasing theoretical and practical applicability. This kind of work began with a split analysis between ‘commercial’ non-profits and what are known as ‘donative’ non-profits.

A good overview of the current and historical research in this vein is provided by Richard Steinberg in his edited book *The economics of non-profit enterprises*. Much of this work sees the rationale for nonprofits as overcoming market failures, for example, by providing public goods or reducing information asymmetries.

It is likely that a full overview of US and US-inspired research might lead to some insights and understandings of useful approaches to the third sector within the UK. However, that work has to recognise the context from which it comes and its scope of applicability:

- most of the US-inspired work relates to organisations that do not distribute profit;
- the UK does not have commercial nonprofits of the same kind or extent of the US, and is equivocal about whether the ones that are similar, are part of the third sector, for example, BUPA;

- a broader question relates to how far different forms of economic analysis can shed light on processes and outcomes of different types of third sector activity, and how much might be excluded by doing so.

Much of the debate on alternative approaches to economics concerns the primary focus of mainstream economic analysis on individual preference maximisation without regard for others or by not incorporating collective action and goods; the nirvana of perfectly clearing markets; and the excessive use of mathematical deductive models.

There have always been alternative approaches to economic discourse which have implications for economic tools and understandings and have had more or less practical relevance in different areas. For example:

- (new) institutional economics
- post-Keynesianism
- behavioural economics
- Austrian neo-Hayekian
- ecological economics “ which particularly seems to have promise for third sector work
- development economics.

These alternative economic analytic approaches are important to consider when looking at third sector activities and understandings since they are based on different behavioural assumptions or conceptualisations which may be more or less suited to different parts of the third sector or different types of action.

There are also potentially useful cross-disciplines and techniques such as:

- political economy
- socio-economics
- geographical economics (Geographical Information Systems and spatial economic analysis and modelling)
- complexity and systems science – recent application to ‘social entrepreneurship’.

UK third sector research on economic aspects of third sector activity has tended to be more practical than theoretical, and also multi-disciplinary.

In addition, new and existing bodies of scholarship provide economic analysis and approaches for different parts of the third sector, for example:

- social entrepreneurship theory and evidence – is eclectic and tends to cover US work on enterprising non-profits as well as more international work on issues such as fair trade, alternative organisational models or supply chains, or social investment;
- grey literature particularly on multi-stakeholder governance models with different forms of limited profit distribution;
- co-operative research;
- employee ownership research;
- social enterprise research – originating from a UK or more European base, focuses more on organisational forms, using concepts of political decision-making and socio-economics, or within different frames such as the ‘solidarity economy’, and tends to stress participatory governance structures;
- possible similarities with business and economic literature which looks at the complex motivations and values of small firms, family businesses and also commercial businesses with non-commercial dimensions or values such as creative or craft-based businesses.

Roles of the third sector within the economy

There has been work on measuring the direct contribution of third sector activities of different kinds to aggregate measures of economic activity such as employment levels, GDP or GVA.

But the impact of the third sector on the economy goes wider. The third sector includes organisations that directly affect market behaviour, structures and activity. These include:

- indirect contributions to the extent and quality of the labour force – for example, job opportunities for the disadvantaged, skill and attitude development;
- economic infrastructure such as workspace or childcare;
- quality of life for inward investment or for employees;
- developing social capital – seen as important for economic impacts such as competitiveness and innovation, job search, trust, or entrepreneurship;
- elements of a working economy – for example, trades unions, professional bodies, organisations for standards setting, sectoral agreements or codes;

- enabling entrepreneurship;
- impact on mainstream corporate social responsibility (CSR) and behaviour;
- helping create ethical markets/ organisations – or more plural economic systems;
- changing people, not just goods and services – altering cultural norms of behaviour and consumer preferences;
- finance provision and innovation.

Beyond market and government failure?

When looking at reasons for government intervention in the third sector, it is difficult to just apply market or government failure. The promotion of local civil renewal or democracy by third sector activity is clearly not a response to market failure. And promoting or encouraging ethical markets and hence inclusion of plural organisational models, is not market failure but about transforming markets.

Conclusions

This Briefing and the related Working Paper only begins to skim the surface of what might be possible within economic analysis for the third sector. In order to progress understanding and choose between potential areas for further in-depth study, several baseline overviews could be carried out. These could include:

- further analysis of predominantly US economic non-profit work for relevance to parts of the UK third sector;
- exploration of alternative and cross-disciplinary economics for possible tools and appropriate theory;
- scoping of the latest economic theory and practice for relevance to furthering third sector understanding;
- overview of economic analysis to date within UK-based voluntary and community sector work;
- exploration of the European social economy model/s for developing theory and practice;
- overview of developing social entrepreneurship and social enterprise theory and evidence (some of this uses mainstream economic approaches such as maximising objective functions, while others question narrow economic theorising);

- overview of co-operative and employee ownership research;
- collection of existing case studies and academic work of boundary crossing social businesses including, for example, John Lewis or the Scott Trust;
- a thorough review of the potential of ecological economics to offer theory and practice to third sector analysis and activities.

In addition, there are particular areas for economic research and economic analysis suggested by this overview including:

- direct third sector engagement in the wider economy – over time and within different sectors and by different models;
- role of third sector activities and values in creating and supporting market frameworks, for example, as regulators, watchdogs, sites for deliberation, trust development, and standard setting;
- innovation;
- comparative and dynamic statics of different models within different sectors against each other and forms of private and public organisations;
- influences of economic and business discourse, language and practices on UK third sector activities and conceptualisations;
- issues of pluralist economic models (in other words, third sector direct involvement) in economies – for example, in static and dynamic resilience (say in relation to economic cycles), inclusion, or for transformation and innovation;
- appropriateness of government economic appraisal and rationales (particularly market failure) of the third sector;
- analysis of third sector involvement in economic and business policy implementation and practice at EU and UK levels;
- impacts on mainstream economic thinking about assumptions and behaviours from third sector economic activities; new or extended concepts of issues such as ‘value’ or ‘productivity’; or ways of incorporating social, economic and environmental resources.

This paper is part of the Third Sector Research Centre – Briefing Paper Series see www.tsrc.ac.uk for more details and a copy of the full Working Paper 14.

The support of the Economic and Social Research Council (ESRC), the Office of the Third Sector (OTS) and the Barrow Cadbury UK Trust is gratefully acknowledged. The work was part of the programme of the joint ESRC, OTS Barrow Cadbury Third Sector Research Centre